ANGEL CAPITAL ASSOCIATION

February 6, 2022

Hon. Janet L. Yellen, Secretary of the Treasury
c/o Himamauli Das, Acting Director, FinCEN
Policy Division RIN 1506-AB49/FINCEN-2021-0005
P.O. Box 39, Vienna, VA 22183

Dear Madam Secretary,

RE: Treasury (FinCEN) Notice of Proposed Rulemaking Titled "Beneficial Ownership Information Reporting Requirements," RIN 1506-AB49, FINCEN-2021-0005, 86 fed. Reg. 69920 (December 8, 2021) (https://public-inspection.federalregister.gov/2021-06922.pdf)

Submitted at https://www.regulations.gov

The Angel Capital Association (the "***ACA***") submits these comments to the Treasury Department's Financial Crimes Enforcement Network in response to its recent Advance Notice of Proposed Rulemaking with respect to the Corporate Transparency Act (the "***CTA***"). By way of background, the ACA is the United States' largest angel investor organization. Members of the ACA invest in thousands of early-stage companies across the U.S. every year. Angels are usually the first non-founder third-party money invested in a company, typically preceding venture capital investment. Angel investors are at the forefront of the U.S. jobs machine, with almost all job growth coming from early-stage companies, the type typically funded by angel investors.

The ACA is intimately familiar with the issues that its members confront as they invest in early-stage and startup companies, and the incidence of money laundering or proliferation or terrorist funding activities amongst companies funded by angel investors and venture capitalists is very, very low.

While we support the objectives of the CTA, the ACA is concerned with unnecessary federal regulation of a segment of the economy that has seen virtually no money laundering, terrorist or proliferation funding, or anything of that nature . Further, this requirement would create a significant reporting burden that many start-up or existing small businesses will struggle or fail to comply with. It appears to us that FinCEN's proposed regulations could be more narrowly tailored to avoid inflicting these reporting obligations on a segment of the economy that sees an extraordinarily low level of the type of activity the rules are targeting.

Accordingly, we have the following recommendations which we believe will improve the proposed rule and minimize unnecessary impact on small businesses:

Extend the Deadline for Making Comments

We urge FinCEN to extend the period for comment on the proposed rules. As proposed, the regulations will have far-reaching and unintended consequences on start-up and early-stage entrepreneurial enterprises, stifling their ability to obtain financing and create jobs. Early-stage companies, especially those funded by angel investors, generate almost all of the net new jobs in

America.[1] The last thing we want to do is stifle the ability of America's technology sector from raising capital, thereby harming workforce growth.

The proposed regulations were released on December 7, 2021, just days before the extended holiday season and amidst the largest infection surge America has faced yet. Comments are due by February 7. 2022, giving little time for those who are impacted by the proposed regulations – such as small business owners – to review, digest and understand the implications the proposed regulations, much less the time to submit their comments.

The proposed regulations are lengthy and impose complex and detailed filing and other requirements on new and existing entities. An extended comment period would allow small business owners, the legal and accounting communities, and other members of the entrepreneurship ecosystem sufficient time to review and comment on the regulations to ensure that they are fair and clear while still accomplishing the important objectives of the CTA.

Entrepreneurs are oftentimes unsophisticated when it comes to the regulatory requirements of launching their new businesses. In addition, not all founders have access to the resources to obtain legal advice on how to comply with complex rules. Frequently founders will form their legal entity without legal or accounting assistance. These founders could easily overlook the requirements of the proposed regulations, creating a liability for their company and making their business less attractive to the investment community, hindering their potential for growth and success. The proposed regulations could thus have a chilling effect on the ability of start-ups and emerging companies to raise capital. The prospect that a company seeking financing has failed to comply with the proposed regulatory filings and other requirements would impede their ability to obtain the capital needed to grow their new business. If these companies inadvertently overlook the complicated filing requirements, the consequences could be severe, and these early-stage businesses could become subject to large fines and criminal prosecution. Because of the severity of the consequences, just the potential that there's been a violation would have to be disclosed to prospective investors, even though the failure to file was completely inadvertent. This could become a red-flag to many investors.

We Think It Is Very Likely There Will Be a Large Degree of Non-Compliance

It is going to take a significant public education effort to make sure founders of new companies, and the management of existing companies understand that there are all sorts of things to be on the lookout for when it comes to compliance with the CTA.

The proposed rules require companies to file an updated report within 30 days after the date on which there is any change with respect to the information previously submitted to FinCEN, starting with the information included in the initial report, ***and*** including any change with respect to anyone who is a beneficial owner of a reporting company ***and*** any change with respect to information reported for any particular beneficial owner or ***applicant***.

Company applicants are frequently just random third parties whose involvement with the company only occurs at the formation of the company and not thereafter. It is a weird requirement to have to tell the company applicant you have to report to FinCEN with 30 days whenever this person moves their address for the life of your company. How do pre-existing entities even obtain this information timely from company applicants when company applicants have no obligation to update the company of their address changes? Many companies are not even going to be able to locate their applicant. We would encourage FinCEN to only require updating applicant information if the applicant has some ongoing role with the company. In other words, what we are saying is you are asking for updates of unrealistic information expectations

[1] NTD: Insert study reference.

that are not practical and are will cause small businesses a lot of time in compliance costs with very little benefit.

For America's small businesses, this whole continuous update regime is going to be a completely new regulatory requirement for America's businesses. There is nothing like what you are proposing that business owners in America currently have to comply with. This continuous reporting regime is more like what public companies have to contend with than what small businesses have to comply with today in America. This is a unique reporting obligation and a dramatically broad regulatory request. Basically, you have 30 days to update your FinCeN filing whenever something changes in your on-file report with FinCEN, including a change in address of company applicants who maybe has had nothing to do with your company for 20 years. Companies are regularly appointing officers and officers are regularly leaving companies as well. The 30-day filing deadline for an update is not a reasonable period of time within which to expect companies to continuously update their officer list with FinCEN.

In addition to making sure that they keep their list of up to date with FinCEN, companies will have to put officers and individual beneficial owners and their directors and company applicants on notice to inform the company if they move their residence, so that their information can be updated with FinCEN within 30 days of their move. Company applicants have no legal obligation to update companies of their address changes for the life of the company's filing obligations with FinCEN.

Many founders and executives and investors take sabbaticals for months at a time. 30 days is not a reasonable expectation for this sort of filing regime on America's smallest businesses.
It is not uncommon for founders to not understand the basic rules of corporate governance, much less these types of continuous reporting regimes like the ones public companies labor under. This is especially the case for founders from underserved communities.

We understand that Secretaries of State will provide founders with information on what is required by the CTA at the time of creating an entity, but almost immediately after an entity is formed an updated filing will be required. This is because it frequently takes more than 14 days for new companies to execute their organizational paperwork in which the board actually authorizes share issuance, appoints officers, adopts bylaws, and founders actually then can sign stock purchase agreements. Accordingly, we feel that the proposed reporting periods here are too short.

What if existing entities cannot obtain the information required to be filed with their initial report? What if the beneficial owners as identified by the company or the company applicant are not available or cannot be reached, or do not understand the importance from the company's point of view of correctly and timely filing the information? What if the "incorporator" of your company that you incorporated 20 years ago cannot be located or is out of the country on sabbatical for the next 6 months or moved out of the country and can't be found?

We understand that Secretaries of State will provide founders information on what is required by the CTA at the time of creating an entity, but the proposed rules contemplate updates whenever the information on file with FinCEN becomes out of date.

If FinCEN goes forward with these regulations, we would encourage FinCEN to design the rules to optimize the likelihood of compliance and reduce and/or eliminate any potential liability for failure to comply completely and correctly with every requirement of the regulations.

The Costs of Compliance Will Be Much Greater Than Estimated

We think that FinCEN is underestimating how much time it will take companies to comply with these rules. You state quite a few times that you do not expect most reporting companies to suffer much of a burden in compliance with these rules. In fact, you say that you believe the amount of additional time and effort required to comply with the proposed rule will be "minimal."

We disagree vehemently on this point.

What is proposed here is a huge new set of compliance obligations on companies. Essentially a whole new area of federal corporate law. Now every time a senior officer resigns, for example, or a senior officer is appointed, or anyone whose information was previously reported to FinCEN moves residence– all these events have to be quickly followed by a filing with FinCEN. Many companies will simply not understand how to comply with the rules. We think in general for compliance purposes it would make the most sense to time the FinCEN filing obligations with the annual reports companies have to file with the state where they are formed. A quarterly filing would even make more sense than what is proposed.

For pre-existing companies the proposed rules require them to gather information that is no longer pertinent or material to who controls them at all (e.g., the company applicant).
The proposed rules impose unrealistic expectations on reporting companies. As the NFIB points out, if a beneficial owner moves their residence, a reporting company is supposed to notify FinCEN within 30 days. This is unrealistic and impractical and a huge intrusion into the private affairs of entrepreneurs and founders and small business owners and the investors who support them.

Attorneys we have polled who represent early stage and startup companies tell us that they expect to have to spend a substantial amount of time with their clients, on an ongoing and continuous basis, to make sure that they do not run afoul of FinCEN's rules. We would urge you to reconsider such frequent updates. It would make more sense for companies to just file quarterly. At least then companies would know with certainty when the filing was due.
The companies that create the most new jobs in America raise money from investors to fund their growth. They hire and fire people regularly. As they grow, they hire more. Many of the people they hire will be considered persons who theoretically might exercise "substantial control." So now it will become a staple of early-stage company governance in America to collect the FinCEN information before hiring or before promotion, and it will drive a divide between company founders with means who are able to hire advisors to assist with compliance, and founders from underserved communities without access to the resource or networks to obtain compliance assistance.

Is Every Director Necessarily A Beneficial Owner?
We are not sure based on the proposed language how to determine which directors of a company are considered beneficial owners.

You say substantial control includes:
"Authority over the appointment or removal of any senior officer or a majority or dominant minority of the board of directors (or similar body);"
Officers of a company are appointed by the entire board of directors, not some subset of the board. Certain groups of shareholders might have a right to appoint a director or two, but even so each director is a fiduciary for all of the shareholders of company, and no one director as the right to appoint or remove any senior officer. It takes a vote of a majority of a quorum or unanimous consent to appoint or remove a senior officer.

Does this mean all directors are beneficial owners?

Also, we are not sure what the meaning of "dominant minority" is.

The Reporting Obligations Will Disproportionately Adversely Affect Underserved Communities

Barriers to entry and regulatory complexity are one of the primary drivers of inequity in the corporate space. While established founders and companies with access to capital and networks may be able to obtain advice and comply with the proposed guidelines, small businesses in underserved communities that do not have access or capital or networks to access advisors to help them navigate this new regulatory scheme will be disproportionately disadvantaged by the proposed rule, and the net effect will be a chilling effect of new businesses formed in these communities, limiting the economic opportunity provided in these communities.

We Need Clarity On Negative Covenants

It is very common in the financing of early-stage companies for equity investors to have what are known as protective provisions, or negative covenants, which serve to protect the core economic expectations of investors. For example, the company cannot go into an entirely different line of business, or sell itself, or sell all or substantially all of its assets, without the approval of holders of a majority of preferred shares. For typical protective provisions, please see the example documents at https://serieseed.com and https://nvca.org/model-legal-documents/

The proposed rules do not say whether negative covenants fall within the meaning of "[D]irection, determination, or decision of, or substantial influence over, important matters affecting the reporting company..."

Most often, a group of individual angel investors invest, and none of them individually own more than 25%, but shares of stock constituting the majority of the shares issued to these investors must approve a sale of the company. In that instance, is every angel investor involved a beneficial owner? Or are none of them?

We note that the proposed regulations generally define creditors as not beneficial owners, and creditors typically have covenants similar to the sort of protective provisions you see in angel financings. We also note that FinCEN regulations say that a person has to exercise substantial control, and it would seem that if a group of angel investors is not being asked to approve anything then they cannot be considered to be exercising any substantial control over the company until perhaps they are actually asked to approve something? Clarity on this issue is needed.

Form D Filers Should Be Exempt

Many early-stage companies file Form D with the Securities and Exchange Commission. The Form D requires that companies disclose their directors and officers, as well as "promoters." The definition of promoter is broad.[2]

Requiring companies that have already filed Form D results in duplicative regulatory burdens. We would ask that FinCEN consider exempting entities that have filed a Form D with the

[2] "**Promoter**" includes:
(i) Any person who, acting alone or in conjunction with one or more other persons, directly or indirectly takes initiative in founding and organizing the business or enterprise of an issuer; or
(ii) Any person who, in connection with the founding and organizing of the business or enterprise of an issuer, directly or indirectly receives in consideration of services or property, or both services and property, 10 percent or more of any class of securities of the issuer or 10 percent or more of the proceeds from the sale of any class of such securities. However, a person who receives such securities or proceeds either solely as underwriting commissions or solely in consideration of property shall not be deemed a promoter within the meaning of this paragraph if such person does not otherwise take part in founding and organizing the enterprise. Securities Act of 1933, Rule 405, 17 C.F.R. § 230.405.

Securities and Exchange Commission to be exempt from the FinCEN beneficial ownership requirements.

The Regulations Need More Clarity
We fear that by imposing a rule set that is difficult for a large number of companies to comply with, FinCEN may be damaging the early-stage ecosystem without any justifying or compensating benefits for doing so. Many startup companies have nominal financial activity for a considerable period of time. It would seem that if FinCEN was truly worried about money laundering it would exempt all entities from this reporting regime unless and until they had more than a nominal amount of financial account activity. For example, a startup funded by founders who each have $50,000 to $100,000 to live on until they have visibility into the viability of their idea are not the people likely to be using their entity to commit money laundering activities. As discussed earlier in this letter, once these companies begin filing reports with the SEC, including Form D, these entities should be exempt from this reporting regime. The incidence of money laundering amongst companies that comply with the Form D filing requirements and are funded through angel groups and venture capital firms is very low.

We believe that the proposed regulations set up to create significant potential liabilities for startup companies and beneficial owners of startup and early stage companies throughout America.

Many business owners will simply not understand the FinCEN rules. Most small businesses are not subject under current law to update any government filing within 30 days lest they want to be subject to fines and penalties. The proposed FinCEN rules are going to be a rude awakening for a lot of business owners.

Making matters worse, it is harder for people without access to advisors to understand that there are a lot of ways they can trigger an update to the FinCEN filings. For example, a company might hire a Vice President. But if the Vice President is deemed to exercise substantial control under the proposed regulations, the FinCEN report is required to be updated. But founders of businesses may not understand that. It would make more sense from a compliance point of view to time the filing of reports with FinCEN to the filing of reports required to be made by entities with the state in which they are formed, as opposed to springing filings obligations that can be triggered simply by day-to-day operations.

We think there are a number of things FinCEN should consider:
(1) Rather than requiring updates within 30 days, how about just requiring quarterly updates?
(2) Frequently a new company does not complete its "organizational paperwork" within 14 days of filing articles of incorporation. After filing a certificate of incorporation, the incorporator of the company has to appoint the initial board, or if the initial board was named in the articles, the initial board of directors then has to hold an initial meeting of the board, at which the board appoints officers, adopts bylaws, and authorizes the initial issuance of shares, pursuant to share purchase agreements approved by the board. Thus, 14 days is too short of time for FinCEN to timely receive the information it wants. Because incorporators will file initial reports and then there will be updates 30 days after the organizational paperwork is complete. Rather, FinCEN might give companies 30 days after their initial shares have been issued or officers appointed (or they have received a threshold amount of funding) to file the initial report. This might result in more compliance and collection of the data that FinCEN wants, and avoid inadvertent and unintentional non-compliance which can have severe and long-lasting consequences
(3) We note that FinCEN's proposed regulations require companies that existed prior to the finalization of these rules to report to FinCEN information from the "incorporator," even if the incorporator has not had anything to do with the company for years. The proposed rules even contemplate what to do if the incorporator has died. This is nonsensical and many companies

will fail to comply with this requirement. For companies already in existence, they should only have to file information for beneficial owners as of the date the rules go into effect, not “incorporators.” Frequently companies will be formed by someone from a third-party formation service provider, accounting firm, or law firm, or ex-founder and they may have no idea of the whereabouts of that person. To give you an example, we know lawyers who have signed hundreds and hundreds of articles of incorporation for new companies over the years, but no longer have any connections to those companies. It is unrealistic to think that all of these companies are going to reach out for FinCEN information. Again, we think you are setting up small business to be widely out of compliance with your rule set.

How to Treat Community Property Interests?
The proposed regulations do not say what to do about a spousal interest in a beneficial interest. In a community property state, property may be titled in the name of one spouse, but the other spouse will own an undivided half interest in that property under the community property law. Do the rules require collecting BOI from spouses in community property states? This is a significant point that should be answered in advance of implementation.

The Definition of Senior Officer is Too Broad
Your definition of senior officer puts small businesses and startups under a more strict reporting regime than public companies in many ways. For example, a public company does not have report on a current basis the appointment of a secretary or a general counsel (unless that person otherwise is in charge of a principal business unit).
The proposed definition of senior officer is too broad:

> *Senior officer.* The term “senior officer” means any individual holding the position or exercising the authority of a president, secretary, treasurer, chief financial officer, general counsel, chief executive officer, chief operating officer, or any other officer, regardless of official title, who performs a similar function.

This definition is too dependent on titles rather than actual authority. A secretary may have no authority whatsoever (this would typically be the case). Similarly, a general counsel may not exercise substantial control over the enterprise.

We think it is unfortunate that FinCEN is going to require the reporting of potentially dozens of officers of reporting companies, when these persons do not in fact exercise substantial control over the entity. Again, this is going to create an ongoing nightmare for America’s fastest growing business until they reach the 20 employee $5m threshold.

$5 Million in Sales Should Include Sales of Equity in a Financing
$5 million in “sales” should include sales of stock or equity to finance a business. This would be consistent with Internal Revenue Code Section 1032.

Concurrence with NFIB Letter
We have additionally reviewed and concur in full with the letter sent by the National Federation of Independent Business (NFIB), dated April 15, 2022, RE: Department of the Treasury Financial Crimes Enforcement Network Notice Titled “Beneficial Ownership Information Reporting Requirements,” Dkt. No. FINCEN-2021-0005, RIN 1506 AB-49, 86 Fed. Reg. 17557 (April 5, 2021)

Conclusion
We are concerned that the proposed regulations will create significant potential liabilities for new and existing companies and their founders throughout America, and have a disproportionate impact on first time small business owners and underserved communities.

Our comments today are in support of both angel investors and the nation's startup entrepreneurs, those who create nearly all net new jobs in the country and many of the innovations that improve the quality of life throughout the world. It is vital that promising startups continue to attract angel capital, for their own growth and for the American economy. We appreciate the opportunity to provide these comments and are available to clarify any of the points listed above. You may reach me at pgouhin@angelcapitalassociation.org or 913-894-4700 X 1.

About the Angel Capital Association

The Angel Capital Association (ACA) is the leading professional association supporting the success of accredited angel investors in high-growth and early-stage ventures. Our 15,000 members are among the angel investors that invest an estimated $25 billion in 70,000 early-stage investments every year, with companies located in every state in the country.

Sincerely,

Marcia Dawood
Chairman, ACA

Pat Gouhin
Chief Executive Officer, ACA